

SOCIAL INVESTMENT PROGRAM (FHIS-3)

(HO-0131)

EXECUTIVE SUMMARY

BORROWER AND GUARANTOR: Republic of Honduras

EXECUTING AGENCY: Fondo Hondureño de Inversión Social [Honduras Social Investment Fund]

AMOUNT AND SOURCE: IDB: (FSO) US\$50.0 million
Local counterpart: US\$ 5.6 million
Total: US\$55.6 million

FINANCIAL TERMS AND CONDITIONS: Amortization period: 40 years
Commitment period: 2.5 years
Disbursement period: 3 years
Grace period: 10 years
Interest rate: 1% during the grace period and 2% thereafter
Inspection and supervision: 1%
Credit fee: 0.5% on the undisbursed amount

BACKGROUND: This operation was originally designed to address the structural causes of the poverty, which affects over half of the Honduran population, who lack the means to meet their basic needs. Close to the end of its preparation, however, a natural disaster occurred in Honduras of a scope unprecedented in the past two centuries. A devastatingly powerful hurricane named "Mitch" blasted the country for three whole days, wiping out much of the progress achieved over the past few years and dramatically increasing poverty among the population.

Based on information compiled by the Bank's emergency mission, there are an estimated 590,000 hurricane victims, 10,000 wounded, 825,000 refugees and evacuees, and over 12,000 people dead or missing. Over 60,000 homes were destroyed and damage to the road system has completely isolated many regions in the country. The World Bank has collected information indicating that most of the water supply systems were completely destroyed and 35% of schools were damaged and consequently closed indefinitely. In addition, over 70% of agricultural production was lost and electric power and telecommunications networks have been severely damaged.

OBJECTIVES: The program is intended to alleviate living conditions for those most in need by restoring and improving access to basic social and economic infrastructure according to priorities established at

the local level. The main challenge the program faces in this connection is to rebuild the infrastructure destroyed following procedures that will contribute substantially to the historic transition toward a new form of cooperation between the central government, municipalities, and communities.

DESCRIPTION:

The proposed program goes to the heart of a historic shift in the relationship between the central government, municipalities and local communities. The great challenge is to implement this new relationship in the context of the urgent process of national reconstruction. This called for a design allowing three-way joint collaboration, without the delays that normally accompany the establishment of new procedures and working relationships. Participatory processes will therefore be gradually introduced depending on the pace at which each municipality overcomes the limitations imposed by the disaster.

The program is divided into three basic components. The first two components consist of investments in a range of activities corresponding to the three phases of response to the destruction wreaked by the hurricane: (i) immediate relief for emergency situations; (ii) short-term investments for reconstruction of basic infrastructure for governability and citizen security; and (iii) medium-term investments for local development, assigned priority by the communities in association with the municipal authorities. Investments in social projects and programs will be carried out in parallel with a strategic study consisting of a series of proposals designed to shape the future operations of the FHIS and address problems which extend beyond the purview and authority of the FHIS, but whose solutions are essential to the effectiveness of FHIS activities. These components are as follows:

1. Investment projects (US\$47.7 million). Emergency activities and investment in reconstruction will be financed through arrangements that will increasingly incorporate the communities in the decision-making process. The component consists of two subcomponents: investments in reconstruction and municipal social investment plans.

Investments in critical reconstruction (US\$33 million): Under this subcomponent, expenses will be financed for immediate relief, including food and medicine, equipment and materials for temporary shelters, mobile latrines and clinics, power generators, and tank trucks for clean water. Basic information will be compiled concurrently to launch the following phase for reconstruction of basic infrastructure. To this end, a technical survey of the damage

caused by the hurricane throughout the country will be conducted immediately. The information compiled in the survey will complement the usual system for targeting resources and will support the process of consultation with each municipality to establish its investment priorities. To achieve maximum community participation during this phase, partial financing will also be provided for a national initiative for community organization and training. Financing will also be provided under this subcomponent for the projects assigned priority during the emergency relief and basic infrastructure reconstruction phases, the duration of which has been set at 12 months.

Municipal social investment plans (US\$14.7 million). In the second quarter of year one of the project, the third phase of the emergency response will be initiated. An innovative procedure for project identification and prioritization, initiation of which had been interrupted by Hurricane Mitch, will be relaunched. In preparing this program, the FHIS had made the special decision to devolve a project portfolio of over US\$140 million to the municipalities. The portfolio had been channeled to the FHIS by the municipalities, without systematic input from the communities. In developing the new portfolio, community workshops and meetings were held throughout the country, in close coordination with the municipalities. The initiative was successful. Over half of the projects in the original portfolio were replaced with others assigned higher priority by the communities. In addition, for the first time the communities were organized to participate actively in local planning. The timing for relaunching the initiative in each municipality will be determined according to its readiness. Financing will be provided for activities to prepare the community meetings and the projects assigned priority by the communities and municipalities in the form of municipal social investment plans.

2. Basic needs (US\$2.2 million). This component targets the most vulnerable groups who require assistance other than that provided for general FHIS beneficiaries. They include the elderly, street children, the disabled, homeless people and ethnic groups. The component is divided into two subcomponents. One, the social welfare component, includes measures ranging from the simple distribution of food to provision of comprehensive child care programs, literacy campaigns, playground equipment, and training for midwives. The other, the training component, contains initiatives that will train program

beneficiaries in sustainability and citizen participation and familiarize municipalities with management aspects. This subcomponent will also include a program called *Nuestras Raíces* ("Our Roots"), which will emphasize the special needs of ethnic groups and finance projects the nature and specifications of which are attuned to the cultural realities of these groups.

3. Strengthening of the FHIS (US\$3 million). In addition to the costs of program administration, resources have been allocated to ensure the quality of the technical team and improve the management systems and operational infrastructure of the FHIS. Training will be provided for the majority of its technical staff, its office equipment and the vehicle fleet will be replaced, and improvements will be made in its management of environmental, maintenance and gender issues.

**ROLE OF THE
PROJECT IN THE
BANK'S COUNTRY AND
SECTOR POLICY:**

The Bank's strategy for Honduras is basically geared towards poverty reduction. To this end, support will be provided for initiatives to improve the equity, efficiency and coverage of public programs, and encourage greater cooperation with the private sector. In the social sectors, the Bank has committed itself to helping the new government formulate a comprehensive social policy which will set priorities and coordinate solutions to problems. One of the ways in which the Bank will help define short- and medium-term social strategy is by actively promoting social policy dialogue. Even so, the level of poverty is such, especially as compounded by Hurricane Mitch, that investment in the sector must continue at the same time as this policy is being formulated. The two most important poverty alleviation programs in Honduras are the FHIS and the PRAF (Programa de Asignaciones Familiares) [Family Allowance Program], and the Bank plans to process operations to support both of them in 1998. The Bank also wishes to play a proactive role in promoting coordination among donors in the area of community development in Honduras. All of the activities designed to address the damage caused by the hurricane are consistent with the Bank's policy on natural disasters.

**ENVIRONMENTAL/
SOCIAL REVIEW:**

In recognition of the need for continuous improvements in the management of environmental issues, an action plan will be implemented for incorporating environmental protection at key stages of the project cycle. In addition, environmental and gender issues will be covered in the training provided for program beneficiaries (paragraph 4.6).

During the previous phase of its operations, the FHIS took important steps to increase participation by women, not only as program beneficiaries but also in its execution. To ensure continuing progress in this

direction, greater participation by women will be sought in managing the planning phase, as well as in project execution and operation. A consultant will be hired to devise initiatives and systems for this purpose, as well as to determine the advisability of including statistics on gender issues in the FHIS management information system (paragraph 4.7).

A significant correlation has been found between pockets of extreme poverty and ethnic groups in Honduras. To address this situation, the special needs of these groups will receive careful attention under the *Nuestras Raíces* subcomponent. And to ensure greater access by these groups to the general operations under the FHIS, the list of projects has been translated in cases where the beneficiaries' native language has a written form, and community workshops will continue to be organized to provide guidance and familiarize beneficiaries with FHIS operations (paragraph 4.8).

BENEFITS:

The program would be initiated at the time of the greatest need for assistance in the wake of Hurricane Mitch. It would help provide a swift response to the emergency (paragraph 1.2).

Provided the line ministries fulfill their commitment to supply the human, physical and financial resources needed for operation of the infrastructure to be built under the program, the respective communities will benefit from a substantial increase in their access to social services (paragraph 4.10).

Transferring the focal point for project identification to the local level will help to create new working relationships between the communities, municipal governments and the FHIS. To bring the point where services are provided as close as possible to where beneficiaries live, new working relationships will be forged at the local level and are expected to produce major efficiency gains in the supply of services. Moreover, communities and municipalities alike will be better organized and trained in devising their own projects (paragraph 4.11).

The new procedures for planning, managing and maintaining the projects will result in greater efficiency and equity in social investment. Moreover, a major positive externality is expected, based on the demonstration effect of more participatory, transparent and efficient procedures that could be followed in the use of municipal resources (paragraph 4.12).

It has been shown that the role of women in promoting the improvement of living conditions for their families is substantially more effective than that of men. Thus, the greater the success of the program in

involving women in project planning and management, in addition to their role as beneficiaries, the greater the impact will be on families (paragraph 4.13).

RISKS:

Transition to the new methodology. The introduction of the new community meeting procedures was interrupted by the hurricane and will be a major challenge to resume in view of the need to expedite corrective measures. This risk will be reduced thanks to technical cooperation to be provided through the Japan Special Fund to lay the foundations for new community meetings and launch investment activities in the first municipalities willing to resume the initiative. In addition, the initiative will be incorporated into the proposed program, since the municipalities may only gain access to the resources for the second subcomponent of the investment project component if they are willing to follow the new procedures (paragraph 4.14).

Transition to decentralization. This program supports the incipient decentralization and community development processes taking place in Honduras. It will therefore be subject to the tensions that normally attend any profound change in a country's economic and political relationships. For example, the government reasoned that FHIS financing could be used in such a manner that it would help the government meet its legal requirement to transfer 5% of tax revenues to the municipalities. However, this approach was contested by the Asociación Hondureña de Municipios [Association of Honduran Municipalities] (AHMON) on the grounds that the law requires such transfers to be made from current tax revenues, and not from external loans. The risk to the FHIS program arising from such tensions will be lessened by the need to work together to address the pressing problems caused by the hurricane (paragraph 4.15).

Joint design. The second component can only proceed if the FHIS, municipalities and communities work together as a team. For example, a project may be included in the FHIS portfolio only if it has been assigned priority by the community, confirmed by the municipality and evaluated by the FHIS. If a municipality or group of communities refuses to participate actively in the program, it will be impossible to achieve the FHIS objectives with respect to that municipality or group. Although this risk is inherent in the cooperative design process, its benefits are sufficient to offset it. Moreover, local training exercises will be carried out, and FHIS activities will be recast in order to make them more supportive and less intrusive (paragraph 4.16).

**SPECIAL
CONTRACTUAL**

Conditions precedent to the first disbursement :

CONDITIONS:

The following must be presented to the Bank's satisfaction:

1. The agreement between the Ministry of Finance and the FHIS for the transfer of the proceeds of the loan and local counterpart contribution to the program (paragraph 3.22).
2. A document constituting the initial report, describing existing measures upon approval of the loan to address the emergency phase. Such measures will comprise: (i) the institutional arrangements to prioritize FHIS activities; (ii) the mechanism to target FHIS investments; (iii) the new items that will be added to the menu; and (iv) the system for priority-setting in each municipality, in order to avoid duplication of efforts with other emergency initiatives and to ensure that project prioritization is delegated to the municipal authorities and local communities. For purposes of this condition, the emergency phase is defined as the 12-month period from the effective date of the loan contract (paragraph 3.3).

Special conditions during program execution:

A revolving fund will be established in an amount equivalent to 20% of the loan amount for the first six months after the effective date of the loan contract, then 10% for the remaining disbursement period, unless the parties agree otherwise (paragraph 3.26).

Within 12 months after the effective date of the loan contract, an expanded version of the operating manual containing the new procedures and responsibilities for community participation in project planning, management, and maintenance will be submitted (paragraph 3.4).

Within 12 months after the effective date of the loan contract, a plan of action for incorporating environmental considerations into key phases of the FHIS project cycle will be submitted (paragraph 4.6).

The terms of reference and detailed specifications will be agreed upon for the program to strengthen FHIS personnel, and for replacement of its equipment and vehicle fleet before resources from the loan may be used for these activities (paragraphs 2.20 and 2.21).

Within nine months after the effective date of the loan contract, the report referred to in paragraph 3.38 must be submitted.

During execution of the program, the payment of honorariums to FHIS technical staff will be subject

to prior agreement with the Bank (paragraphs 2.22 and 3.19).

In addition to the standard clauses, the loan contract will include provisions for auditing, progress reports, inspections, procurement of goods and services, and maintenance services.

**POVERTY TARGETING
AND SOCIAL
CLASSIFICATION:**

This program qualifies as a poverty targeted investment (PTI) since it provides support for a social investment fund (paragraph 4.9).

**EXCEPTIONS TO
BANK POLICY:**

See section on procurement below regarding the procurement of vehicles.

**PROCUREMENT OF
GOODS AND
SERVICES:**

During the emergency period, as defined in this program, the Bank's emergency procurement procedures will be followed, incorporating the flexibility necessary to address the distortions caused in supply and construction markets by Hurricane Mitch. The emergency procedures are as follows: international competitive bidding will be required for: (i) the purchase of goods in amounts equal to or greater than US\$350,000; (ii) the awarding of construction contracts in amounts equal to or greater than US\$3 million; and (iii) the hiring of consulting services in amounts above US\$200,000. The procurement of goods and services in amounts below these thresholds will be carried out in accordance with FHIS procurement manuals. No cap has been established for direct hiring (paragraph 3.35), and a mission will be carried out within six months after the effective date of the loan contract to determine whether this decision should be changed (paragraph 3.40). Execution on force account will be allowed for certain projects provided that: they are not part of the negative list agreed upon with the Bank; they do not exceed 15% of FHIS reference prices; they are used for programs that will provide income to groups affected by Hurricane Mitch; and the total value of such projects does not exceed 15% of the program resources (paragraph 3.36).

For the period following the emergency phase, standard Bank procedures will be followed: international competitive bidding for works in amounts equal to or greater than US\$1.5 million and for the purchase of goods in amounts equal to or greater than US\$250,000. For amounts below these thresholds, see the table in paragraph 3.34.

There is a confirmed need to replace most of the FHIS's vehicle fleet so that it can carry out the duties assigned to it under the program more efficiently. It is recommended that international bidding for partial replacement of the fleet be limited to suppliers of the make of vehicle selected

under the earlier bidding procedures
(paragraph 3.31).